

Department of the Treasury

Internal Revenue Service
Western Area (7/GE)

2 Cupania Circle
Monterey Park, CA 91755-7431
[REDACTED]

Date: FEB 09 2000

Employer Identification Number:
[REDACTED]

DLN:
[REDACTED]

Person to Contact:
[REDACTED]

Special Identification Number:
[REDACTED]

Telephone Number:
[REDACTED]

Fax Number:
[REDACTED]

CERTIFIED MAIL

Dear Applicant:

We have considered your application for exemption from income tax as an organization described in section 501(c)(3) of the Internal Revenue Code.

The information submitted discloses that you were incorporated on [REDACTED] on [REDACTED]. The specific purpose of your organization, as stated in your Articles of Incorporation, reads in part as follows: "...to establish and maintain a safe residential living environment for people with developmental disabilities".

You amended your Articles of Incorporation on [REDACTED] in order to comply with the provisions necessary to meet the requirements as described under section 501(c)(3) of the Internal Revenue Code.

You requested non-private operating foundation status as an organization described in sections 509(a)(1) and 170(b)(1)(A)(vi) of the Internal Revenue Code.

The activities of your organization according to your Form 1023 are to act as a supported living agency, to provide a residential program for people with developmental disabilities in a clean, safe, and healthy environment, to promote the development and implementation of new techniques and program approaches, to ensure opportunities for positive change and personal growth and development, etc. These goals will be accomplished by providing 24 hours-direct care staff.

FACTS:

The organization has developed an organization structure, admission policy and procedures, resident rights, resident termination, management of resident funds and possessions, personnel policies and duties, etc.

In the organization's admission policy it considers the following individual characteristics:

- a. Age compatibility with other clients;
- b. Developmentally disabled;
- c. Meets the criteria of organization's professional care agreements;
- d. Exhibits no behavioral disorders, erratic actions which places himself/herself and/or other risk of significant physical harm or abuse;
- e. Is judged to require long term care residential services as most appropriate and least restrictive option.

Determination will be made by the Board of Directors, Manager, and one direct care staff that the organization can meet the clients needs.

Each resident will have an individual service plan that addresses specific health needs. This includes a nurse (RN) oversight through the Medicaid personal care.

The home will accommodate clients and a live-in caregiver. The house has bedrooms and bathrooms.

The organization was developed because of a need for residential services for young men with developmental disabilities. The of these young men decided they could develop a program that was more cost-effective and provided better care for and other developmentally disabled adults. In the process of developing the organization, the came across a program through that gave loans to people with disabilities to purchase homes through qualifying on. It would give each resident more stability, a place in his local community, and pride of ownership. The organization would manage and support the home.

Each resident is part owner of the property (like a co-operative) which allows him to feel secure and safe from being unnecessarily discharged from the residence.

The Board of Directors consists of 9 individuals, which includes each plus unrelated individuals. Each is an officer of the organization.

The organization is funded from at the daily rate of \$ per client. The organization estimated that % of the expenditures were for wages and taxes and % for administrative and related expenses. Fundraising will be used to provide additional recreational needs, equipment, or repairs if the income is insufficient to cover expenses.

ISSUE:

Does the organization qualify for exemption as an organization described in section 501(c)(3) of the Internal Revenue Code?

LAW:

Section 501(c)(3) of the Internal Revenue Code describes certain organizations exempt from income tax under section 501(a) and reads in part as follows:

"(3) Corporations, and any community chest, fund, or foundation organized and operated exclusively for religious, charitable, scientific, testing for public safety, literary or educational purposes, or to foster national or international amateur sports competition (but only if no part of its activities involve the provision of athletic facilities or equipment), no part of the net earnings of which inures to the benefit of any private shareholder or individual, no substantial part of the activities of which is carrying on legislation, (except as otherwise provided in subsection (h)), and which does not participate in, or intervene in (including the publishing or distribution of statement), any political campaign on behalf of any candidate for public office."

Section 1.501(c)(3)-1(a)(1) of the Income Tax Regulations provides that in order to be exempt as an organization described in section 501(c)(3), an organization must be both organized and operated exclusively for one or more of the purposes specified in such sections. If any organization fails to meet either the organizational test or the operational test, it is not exempt.

Section 1.501(c)(3)-1(b)(1)(i) of the Regulations provides that an organization is organized exclusively for one or more exempt purposes only if its articles of organization (a) limit the purposes of such organization to one or more exempt purposes; and (b) do not expressly empower the organization to engage otherwise than an insubstantial part of its activities, in activities which in themselves are not in furtherance of one or more exempt purposes.

Section 1.501(c)(3)-1(c)(1) of the Regulations provides that an organization will be regarded as "operated exclusively" for one or more exempt purposes only if it engages primarily in activities which accomplish one or more of such exempt purposes specified in section 501(c)(3). An organization will not be so regarded if more than an insubstantial part of its activities is not in furtherance of an exempt purpose.

Section 1.501(c)(3)-1(d)(ii) of the Regulations states that an organization is not organized or operated exclusively for one or more exempt purposes unless it serves a public rather than a private interest. Thus, to meet the requirements, an organization must establish that *it is not organized or operated for the benefit of private interest, such as designated individuals, the creator or his family, shareholders of the organization, or persons controlled, directly or indirectly, by such private interests.*

In Presbyterian & Reformed Publishing Co. v. C.I.R., 79 T.C. 1070 (1982), the Tax Court found that the manner in which the organization conducted its activities revealed a nonexempt commercial purpose that was substantial in nature. In making this determination, the court noted that whether an organization satisfies the operational test is essentially a question of fact. The court noted that where a nonexempt purpose is not an expressed goal of the organization, courts have nonetheless focussed on the manner in which the organization conducts its activities, implicitly reasoning that and can be inferred from the means chosen to attain it. If, for example, an organization's management decision replicate those of commercial enterprises, it is fair to infer that at least one purpose of the organization is commercial.

[REDACTED]

The Supreme Court stated in Better Business Bureau v. United States, 326 U.S. 279, 66 S. CT. 112, 90 L. ED. 67 "...the presence of a single [non charitable] purpose, if substantial in nature, will destroy the exemption regardless of the number of importance or truly (charitable) purposes."

See Church of Boston V. Commissioner, (1978) 71 T.C. 102; Colorado State Chiropractic Society, (1989) 93 T.C. 487; Best Lock Corporation, (1959) 31 T.C. 1217; St. Louis Science Fiction Limited v. Commissioner, T.C. Memo 1985-162 and Minnesota Kingsmen Chess Association Inc. v. Commissioner, T.C. Memo 1983-495; all of these court cases held that the presence of a single non-exempt purpose and a substantial non-501(c)(3) activity results in loss of exemption despite the presence of other exempt purposes.

Revenue Ruling 67-5, 1967-1 CB 123, states that a foundation controlled by the creator's family engaged in financial activities which are beneficial to them is determined to operate for a substantial non-exempt purpose and serving the private interests of the creator and his family. Therefore, the organization is not entitled to exemption from Federal income tax under section 501(c)(3) of the Internal Revenue Code.

Revenue Ruling 69-175, 1969-1 CB 149, held that an organization formed by parents of pupils attending a private school that provided school bus transportation for its members' children served a private rather than a public interest. Revenue Ruling 69-175 states, in pertinent part, as follows: "When a group of individuals associate to provide a cooperative services for themselves, they are serving a private interests".

ANALYSIS:

All of the preceding Code sections, Regulation sections, Revenue Rulings and court cases describe the criteria under which an organization may be exempt under section 501(c)(3) of the Internal Revenue Code. They also describe the basis for which organizations were denied exemption because they were not organized and operated exclusively for section 501(c)(3) purposes, but for the private benefit of their related family members.

Under section 501(c)(3) of the Code, organizations who are not operated exclusively for one of the specified purposes of section 501(c)(3) or organizations whose sole purpose is providing private benefit to its members or individuals are not exempt under section 501(c)(3) of the Code. Your organization's activities serve private rather than public interests. The disbursement of the organization's funds to pay [REDACTED] indicated a private gain for [REDACTED]. The organization formed and operated as a cooperative or mutual benefit for the [REDACTED]. The selections of the recipients are [REDACTED]. This appears to be a private interest and more than just an incidental activity.

You have a substantial non-exempt purpose of assisting [REDACTED] and operate primarily to serve the private interests of your [REDACTED]. You are not "operated exclusively" for an exempt purpose pursuant to section 1.501(c)(3)-1(c)(1) of the Regulations. You did not satisfy the Service that you meet any of the exempt purposes as described under section 501(c)(3) of the Code.

CONCLUSION:

To be considered for tax exempt status under section 501(c)(3), an organization must be both organized and operated exclusively for one or more of the purposes specified in that section. Also, its activities must be restricted to those permitted a section 501(c)(3) organization.

It is the position of the Internal Revenue Service, based on the information submitted, that you are not entitled to exemption from Federal income tax as an organization described in section 501(c)(3) of the Internal Revenue Code, inasmuch as you are not organized and operated exclusively for any of the specified purposes within that section. You are organized and operated exclusively for the private benefit of your members.

If you are in agreement with this proposed determination, we request that you sign and return the enclosed agreement Form 6018. Please note the instructions for signing on the reverse side of the form.

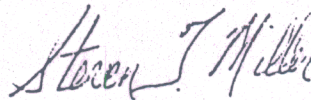
If you disagree with this proposed determination, we recommend that you request a hearing with our office of Regional Director of Appeals. Your request for a hearing should include a written appeal giving the facts, law, and any other information to support your position, as explained in the enclosed Publication 892. You will then be contacted to arrange a date for a hearing. The hearing may be held at the office of Regional Director of Appeals or, if you request, at a mutually convenient District Office. A self-addressed envelope is enclosed.

If we do not hear from you within 30 days from the date of this letter, and you do not protest this proposed determination in a timely manner, it will be considered by the Internal Revenue Service as a failure to exhaust available administrative remedies and will then become our final determination.

Section 7428(b)(2) of the Internal Revenue Code provides in part that "declaratory judgement of decree under this section shall not be issued in any proceeding unless the Tax Court, the Claims Court, or the district court of the United States for the District of Columbia determines that the organization involved has exhausted administrative remedies available to it within the Internal Revenue Service."

If you have any questions, please contact the person whose name and telephone number is shown in the heading of this letter.

Sincerely your,



Steven T. Miller
Director, Exempt Organizations

Enclosures:
Form 6018
Publication 892
Notice 1214
envelope

Department of the Treasury-Internal Revenue Service
CONSENT TO PROPOSED ADVERSE ACTION
(All references are to the Internal Revenue Code)

Prepare In
Duplicate

Case Number

Date of Latest Determination Letter

Employer Identification Number

Date of Proposed Adverse Action Letter

Name and Address of Organization

I consent to the proposed adverse action relative to the above organization as shown by the box(es) check below. I understand that if Section 7428, Declaratory Judgments Relating to Status and Classification of Organizations under Section 501(c)(3), etc. applies, I have the right to protest the proposed adverse action.

NATURE OF ADVERSE ACTION

☒ Denial of exemption

☐ Revocation of exemption, effective

☐ Modification of exempt status from section 501(c)() to 501(c)(), effective

☐ Classification as a private foundation (section 509(a)), effective

☐ Classification as a non-operation foundation (section 4942(j)(3)), effective

☐ Classification as an organization described in section 509(a)(), effective

☐ Classification as an organization described in section 170(b)(1)(A)(), effective

If you agree to the adverse action shown above, please sign and return this consent. You should keep a copy for your records.

If you sign this consent before you have exhausted your administrative appeal rights, you may lose your rights to a declaratory judgment under section 7428.

(Signature instructions are on the back of this form.)

Name of Organization

Signature and Title

Date

Signature and Title

Date